SHOULD THE MANUFACTURER HAVE THE RIGHT TO FIX SELLING PRICES?

By Gilbert H. Montague,
Counsellor at Law, New York.

If a categorical answer be required to this question, it will have to be, Yes—and No. For many different things may be meant by this question: some deserving indisputably the answer Yes; some receiving, by universal consent, the answer No; and many more presenting considerable difficulties in the way of any answer whatsoever.

I

Everyone probably will agree that the manufacturer has, and should have, the right to set the prices on his own goods to his own immediate customers. Everybody who sells anything has always had this right. Nobody, therefore, would now deny it to the manufacturer.

But ought the manufacturer to be allowed to reserve to himself the right to set the price at which his goods shall be sold by his customers to their customers, and by his customers' customers to their customers, and so on down the line of trade that begins with the manufacturer, and ends when the last retailer parts with his goods to the ultimate consumer?

The general run of people who sell things, it is admitted, do not claim any such right. Most people, indeed, not only omit to claim it but appear to get along quite contentedly without it. A considerable amount of popular and governmental and judicial opinion, also, appears to be somewhat loosely to the effect that people, perhaps, do not have any such right.

Why then do certain manufacturers want it? And are there any good reasons why any manufacturer needs it any more than other people?

Manufacturers generally do not feel the need of any such right. But manufacturers of trade-marked and branded goods advocate it as a business necessity.

Why does the manufacturer of popular trade-marked and

branded goods want this right? And why does he need it any more than manufacturers of other goods, or the general run of people who sell things?

II

Trade-marked and branded goods have certain distinctive characteristics. They are articles taken out of a general class of goods, and sold on their peculiar merit. Possessing but a limited field within a single commodity, their cost of distribution is practically prohibitive, unless they are consumed in large volume. Large volume, however, requires national distribution, and national distribution can be effected only by a selling plan which is reasonably economical. The cost of country-wide salesman solicitation, in the case of all excepting the most expensive articles, is absolutely prohibitive. National advertising is the only means for meeting this difficulty. It is, indeed, the most modern method of economical distribution. But it is feasible only when the remainder of the distributing system is subject to practical commercial methods.

Trade-marked and branded goods must, to some extent, be standardized. For unless the trade-mark and brand are associated in the public mind with some definite standard, they are either meaningless or positively detrimental. The standard signified by the trade-mark and brand must also meet the competition of rival standardized and unstandardized goods. Goods that are unique, or unstandardized, or not readily comparable with other goods of the same general class, or that are the subject of monopoly, or for any other reason are not subject to competition, do not need trade-marks and brands. Only when the commodity is a standardized member of a general class, and is controlled by some one who does not control the rest of that class, and is sold in competition with rival goods—in other words is a specialty—does it need a trade-mark and brand. The trade-mark is the manufacturer's guarantee of quality.

Trade-marks and brands, indeed, are the true badges of business competition. They are designed to ear-mark standardized goods that otherwise might not be easily distinguishable from the mass of goods with which they compete, and to differentiate them by name and dress from all goods controlled by rival manufacturers, and to identify them and single them out from among the mass of goods of the same general class. By their trade-marks and brands, all lines of business reflect the degree to which they are truly competitive. Trade-marked goods make for intensive competition.

Competition is the reason for trade-marks and brands. But wherever trade-marks and brands have become firmly and favorably fixed in the public mind, and figure in the marketing of goods, they have, to a degree only recently appreciated, revolutionized the old-fashioned business competition.

III

The Old Fashioned Method

Competition among manufacturers of untrade-marked and unbranded goods—the old-fashioned business competition—began and ended with manufacturers' immediate customers—a more or less local business.

By them—a select audience, mostly of a few wholesalers, all more or less expert judges—the goods were weighed and considered as to price and quality, and the reputation for reliability and good service and all the other elements in the personal equation of the manufacturers ended there. When their decision was made, and the goods were purchased, these wholesalers, in turn, in competition with each other, submitted to the larger and less expert audience of their customers the price and quality of the goods. Into this transaction there entered little of reputation for reliability and good service and all the other elements in the personal equation, and what did enter was *not* of the manufacturer from whom the wholesalers had purchased but of the wholesalers themselves. These wholesalers' customers, having weighed and considered as best they could all these considerations, and having made their decision, and having purchased the goods, thereupon submitted, in turn, in competition with each other, to the still larger and less expert audience of their customers, the price and quality of the goods, and the reputation for reliability and good service, *not* of the manufacturers who made the goods, nor yet of the wholesalers from whom they purchased them, but the reputation for reliability and good service and all the elements in the personal equation of—themselves. Thus it ran down the line of trade, until the last retailer had parted with the goods to the ultimate consumer. The dealers, in a phrase, were at each step selling their own goods on their own reputation.

No other course, indeed, in the case of untrade-marked and unbranded goods was possible. Since the goods were not identified by trade-marks and brands, the manufacturer could not, except in dealing with his immediate customers, ear-mark the goods among

all the others of the same general class or differentiate them from rival goods, or single them out for special and widespread commendation. In a very real sense, the manufacturer had not, and could not have, any interest in the goods after they had left his hands, nor any effective part in any sale beyond that which he himself had made to his immediate customers. Prices fluctuated widely, especially to the consumer; and the aggregate increase of price from manufacturer to consumer is inevitably very great under this system.

IV

Modern Methods of National Distribution

All this has been changed, however, wherever trade-marks and brands have become firmly and favorably fixed in the popular mind, and have begun to figure in the marketing of goods.

Competition among manufacturers of such goods—the new fashioned business competition—begins as usual with the manufacturer's immediate customers, but it ends only with the ultimate consumer of the goods.

Such a manufacturer's immediate customers are mostly wholesalers, but they are always more or less expert judges of the goods; and, just as in the case of untrade-marked and unbranded goods, they can always weigh and consider their price and quality, and the reputation for reliability and good service and the other elements in the personal equation of the manufacturer. But when their decision is made, and the goods are purchased, and these wholesalers, in turn, offer them to their customers, they appeal to an audience which is in quite a different mood from that which judges untrade-marked and unbranded goods. The appeal, under the modern method, is also supplemented by the direct and continuous efforts of the manufacturer himself, to stimulate demand by national advertising, retail solicitation, and other means.

If the trade-mark and brand has become firmly fixed in the public mind, no customer to whom the wholesalers can appeal can be wholly ignorant of the quality of the goods. If the goods have endured the notoriety of their trade-mark and brand without perceptible diminution of sales, it is probable that the customer is measurably convinced at the very outset regarding the quality of the goods, and the reputation for reliability and good service and

all the other elements in the personal equation of the manufacturer. If to this knowledge be now added knowledge of price—the most obvious and frequently best known fact of all, upon which depends the whole question we are considering—and if this also is measurably satisfactory, then practically every factor determining in a sale is already favorably active in the customer. The price is stable; and with a normal and increasing demand and regularity of consumption, a low margin of profit prevails and the increase in price to both manufacturer and consumer is greatly lessened, as compared with the old fashioned method. Thus the wholesalers are relieved,for the most part, from the necessity of assuring their customers regarding the price and quality of the goods, and the reliability and responsibility of the manufacturer, and need assume, indeed, practically no risk or responsibility whatever in respect of the goods. At every point in the line of trade, until the last retailer parts with the goods to the ultimate consumer, the same condition obtains. The prospective purchasers at each stage, instead of being, as in the case of untrade-marked and unbranded goods, progressively less expert and less convinced of the price and quality of the goods and more suspicious of the reliability and responsibility of the manufacturer, are, in the case of trade-marked and branded goods, already familiar with the goods, at least by reputation, and fairly well convinced of their price and quality, and generally well satisfied of the reliability and responsibility of the manufacturer, and practically need no assurances whatever on any of these points from the dealers handling the goods. Competition among a few individual merchants has thus been largely transformed, and vastly increased, and become national competition among rival trade-marked goods. But unreasonable prices cannot prevail, because the manufacturer's interest must hold them low. His profits come from increased volume, not from increased price.

The suction power of the consumers' desire, that draws the goods swiftly through the hands of wholesalers and retailers and immediate dealers of every variety and into the hands of the ultimate consumers, the preconceived conviction of the prospective purchasers in favor of the goods at every stage along the line, the fortification of innumerable places where the consumers' judgment or whim might otherwise break down the line—all of which the manufacturer himself, unaided except by his own labor and capital,

creates by aggressive popularization of his trade-mark and brand—all these are forces as real and potent as physical laws. In the poverty of our language, these forces are collectively called by the rather weak names of "good will" or "popularity."

In most instances today, this popularity is in no small measure the result of wise and extensive advertising. But this is only because advertising is today the least costly way by which the manufacturer can firmly and favorably fix in the public mind, or, for that matter, in the mind of any one with whom he is not already dealing as an immediate customer, the trade-mark and brand that identifies his goods among all the others of the same general class, and distinguishes them from rival goods, and by which alone he can single them out for special and widespread commendation. This puts the highest premium on the integrity of the goods, is a guarantee of satisfaction, and an insurance of a reasonable price which cannot be increased.

The significant thing is that, in a very real sense, the manufacturer of such goods, by the popularity with which he has vested his trade-mark and brand, and by his continued advertising and methods to develop increased demand for his particular goods, continues to play a most effective part in every sale of the goods, down to the final sale of the last retailer to the ultimate consumer.

V

The Problem is: What is the Most Effective and Economical Method of National Distribution?

To expand this proposition would be very attractive. But adequately to do so would swell this article into a history of the most stupendous improvement in distribution that has occurred since the days of Adam Smith. To give even the most obvious illustrations would require narrating the prodigious development of country-wide marketing plans and national selling organizations that have brought into common use scores of special brands and have made household words of hundreds of trade-marks. It is a fascinating chapter of economic history, entirely due to American enterprise, and of which popular and governmental and judicial opinion ought to be appreciative and proud; but the only points which there is now time to extract from it are these:

In a very real sense, the manufacturer of popular trade-marked and branded goods *sells* them, not only to his immediate customers,

but also to their customers, and their customers' customers, and so on down the line to the ultimate consumer; and in this respect the manufacturer of popular trade-marked and branded goods differs entirely from the general run of people who produce and sell things.

VI

Here, then, is the elemental reason why the manufacturer of popular trade-marked and branded goods feels the necessity and claims the right to fix the selling price beyond his immediate customers:

To the extent that he practically sells his goods at each successive stage of the line of trade down to the ultimate consumer, he claims the right, that everybody else has always had, to fix the price on his own goods to all his customers.

All other reasons are corollary to this, and spring from this central fact. The manufacturer has an interest in the success of his particular goods, to the extent of the grand total of volume of sales of all the dealers handling them. Each dealer has an interest in their success only to the extent of the relatively small quantity he handles. The manufacturer has his constant expenses for advertising and solicitation, to increase the volume of their distribution. The wholesalers and retailers do not have this burden. Yet it operates for their benefit. This extra cost, moreover, is not passed on to the public, for the price is already fixed. The manufacturer absorbs this extra cost, if successful, because his increased volume permits a lessened cost per unit. Since the manufacturer assumes all this burden, and the consuming public does not have its price increased, it is in the public interest to permit the manufacturer to use every reasonable means to expand his business for the sake of his more effective competition with other brands.

Price cutting of untrade-marked and unbranded goods at most affects only a small field, and a narrow interest, namely, the price cutter's competitors, and the purchasers to whom the cut prices are offered. Since such goods are unstandardized, and not readily comparable with others of the same general class, the price cutter's competitors have almost as good an opportunity as before to avail of their reputation among their trade for reliability and good service and all the other elements in their personal equation, and thereby to preserve general confidence in the prices and quality of the goods upon their shelves. Since the goods are unidentified by trade-marks

or brands, any verdict which the price cutter's customers or the customers of his competitors may express cannot prejudice other dealers handling the same goods elsewhere in their struggle to obtain the popular verdict for efficiency. Nor can it embarrass the manufacturer of the goods. For he has no effective part in any sale beyond the sales which he himself has made to his immediate customers. Except in the mind of this restricted audience, he is not at all associated with the goods.

VII

Price cutting of trade-marked and branded goods, however—that is, cutting below the prices which the manufacturer has familiarized in connection with his trade-marks and brands—affects not only the price cutter's competitors and their immediate purchasers but also everyone in the line of trade on the particular goods, up as high as the manufacturer himself, and down as far as the ultimate consumer. It affects the entire national distribution of a standard article.

Since such goods are all ear-marked and standardized, and their price and quality have been familiarized by their trade-marks and brands, there can be no question of their quality, and any appeal by the price cutter's competitors to their reputation in their trade for reliability and good service and all the other elements in their personal equation as dealers cannot overcome the difference in price. Against cut prices on trade-marked and branded goods the price cutter's competitors can present no argument. Until they throw out this line of goods, and take up another, the cut price stultifies every justification they can advance for the old price, and even threatens their good will and actual existence.

Under these circumstances, the capture of the customers of the price cutter's competitors is seldom due to any enduring efficiency on the part of the price cutter. More often, it is only a sudden raid, timed by the price cutter so as to produce the greatest possible demoralization and stampede of his competitor's trade, not only in the line on which he is cutting prices, but also in all other lines, and executed at a large initial loss to the price cutter, in the confidence that under cover of the resulting demoralization and stampede, he can more than recoup upon other lines. So immediate and so deadly is this kind of price cutting that if a price cutter misses killing

his competitor—whom he generally aims to kill whenever he resorts to this kind of price cutting—he not infrequently kills, and always seriously hurts, the manufacturer, toward whom the price cutter, to give him credit, seldom has any real ill feeling whatsoever. For to the extent that the manufacturer has popularized his trade-mark and brand and developed a volume of trade, he suffers from such price cutting. He suffers the moment that jobbers and retailers, being affected by the price cutting of others, are unable to handle the goods at a profit, and cease to handle them at all. The manufacturer's own ability to distribute economically then ceases. Save in the case of certain high-priced articles, he cannot nationally distribute his goods direct to consumers, except by a vastly increased cost as compared with the normal basis. Since the goods are all identified by trade-marks and brands, the sensation, which the price cutter creates at the expense of his competitors, fixes in the minds of purchasers in general a depreciated price for the goods on the shelves of all other dealers who handle them, and prejudices every dealer in his struggle to obtain among his own trade the reputation for being an efficient and reliable dealer. Dealers everywhere, therefore, begin to avoid the goods like pestilence; and through the resulting loss in reputation of the goods, among dealers and purchasers everywhere, the manufacturer's business is always seriously hurt, and not infrequently is killed.

VIII

The manufacturer and the price cutter's competitors are not the only sufferers from price cutting of popular trade-marked and branded goods.

Popularity, as every manufacturer and dealer knows, must be based upon fair and reasonable prices—"goods worth the money"—and upon their merit. For only goods of demonstrable merit can survive the test of widespread use. Goods that are meritorious, and, therefore, popular, are frequently driven from the market by price cutting. Goods of doubtful merit, or indifferent popularity, which legitimately might be selected for price cutting because their lack of merit and popularity ought to be made up by a cut in price, are more often the substitutes which the price cutter foists on the public at prices far in excess of their merit, by which he recoups his losses from price cutting.

Under the spell of a temporary saving, therefore, the public is gulled into a worse bargain, and eventually loses, also, the opportunity of buying anywhere the meritorious and once popular trade-marked and branded commodity, that has been driven from the market by price cutting.[1]

IX

Cessation of such price cutting on trade-marked and branded goods will probably not bring the millennium. Dealers will always fail in business on account of deficient salesmanship and bookkeeping and management and other elements in their personal equation. Whether price cutting continues or ceases, however, price cutting of popular trade-marked and branded goods is undoubtedly a ready and frequently used weapon of predatory business, which yields practically no enduring good to purchasers, and invariably causes lasting injury to manufacturers and to dealers handling the goods who lie far outside the price cutter's field of competition or even comprehension, and whose ruin brings no corresponding advantage to the price cutter, nor to the community, nor to any one else. What the manufacturer of trade-marked goods needs is the means to assure to all dealers fair remuneration for the service of constantly carrying and distributing his goods. Price plans, setting reasonable standard prices, have this effect, and are required. But they can be commercially maintained only when the compensation is fair, and neither unduly high nor unduly low.

X

The economic problem that confronts the manufacturer of popular trade-marked and branded goods who tries to fix prices beyond his immediate customers—independently of any legal difficulties—effectually removes every possibility of abuse of price standardization.

Only in proportion as his efforts have firmly and favorably fixed his trade-marks and brand in the public mind will there be any inducement to enter into any such arrangement. And only

[1] On this, and many other phases of this question, see the testimony, documents and articles referred to and collated in "Hearings before the Committee on Interstate and Foreign Commerce," House of Representatives, Sixty-third Congress, Second and Third Sessions on H. R. 13305: "To Prevent Discrimination in Prices and To Provide for Publicity of Prices to Dealers and the Public," February 27, 1914 to January 9, 1915.

when the merits of his commodity outweigh the restrictions of the arrangement, and the benefits of both outweigh the quality and the terms which his competitors all offer, can he ever induce any one to enter into a price arrangement with him. Trade-marked and branded goods and price arrangements, that can successfully run the gauntlet of all these considerations, will be neither so numerous nor so unreasonable as ever to disturb the peace of those who now inveigh against price standardization.

XI

But the law, were it exactly as conservative advocates of price standardization desire, would still prevent every possibility of abuse.

Merely placing upon patented goods a notice that they shall not be resold at less than a specified figure has been held by the Supreme Court of the United States to be ineffective.[2] Whether any patent restriction can be devised that will effectively fix the resale price is a question which the District Courts of the United States are still discussing.[3] Laying aside the question of patents, however, and relying simply on the economics of their situation, many manufacturers of popular trade-marked and branded goods claim the right to contract with their immediate customers regarding the price at which such customers in turn shall sell to their own customers; and some, indeed, go further, and claim also the right to contract regarding the price at which the last retailer shall sell to the ultimate consumer.

Because some of the earlier cases, involving price fixing contracts, appeared, in view of the surrounding circumstances, to show a restraint of trade and a tendency toward monopoly, the courts in some of these cases held that these particular contracts were unenforceable on grounds of public policy.[4] But under other circumstances, that would plainly preclude every possibility of restraint of trade and monopoly, it is hardly believable that contracts regarding resale prices, voluntarily entered into by the purchasers themselves, ought to be held to offend against public policy. Con-

[2] Bauer *v.* O'Donnell, 229 U. S. 1.

[3] Ford Motor Company *v.* Union Motor Sales Company, D. C. S. D. Ohio, December 4, 1914, 225 Fed. 373; American Graphaphone Company *v.* Boston Store, D. C. N. D. Illinois, September 3, 1915, 225 Fed. 785.

[4] Miles Medical Company *v.* Park and Sons Company, 220 U. S. 373.

sidered commercially, they simply give to each dealer, in the manufacturer's distributing system, a reasonable and regular compensation for service rendered. Since the manufacturer himself, had he only sufficient capital, could sell direct to the ultimate consumer, certainly any system by which he can nationally distribute his articles more economically than by direct selling should be permissible; particularly when such system utilizes usual and regular channels of wholesale and retail distribution, and preserves as independent business units tens of thousands of wholesale and retail merchants, whose business has been built up through years of earnest effort.

In highly competitive business, where trade-marked and branded goods most abound, the purchasers themselves can generally be trusted not to enter into bargains that will unreasonably restrict themselves. So long as the field is kept open to other and competing lines of trade-marked and branded goods, the possibility of restraint of trade and monopoly would seem to be practically negligible.

In highly competitive business, indeed, it is today almost impossible to market a specialty without insuring dealers against loss by price cutting. So that unless the manufacturer of a trade-marked and branded specialty, struggling against competition and pushing his line through the regular channels of wholesale and retail distribution in the direction of popular favor, can make some arrangement with wholesalers and retailers to guard against price cutting in his line, he will have to withdraw from the contest, and abandon the field to richer manufacturers, who alone have the capital and organization to dispense entirely with the wholesale and retail trade, and alone can afford to establish branches, employees and agents in every hamlet and sell at their own prices directly to the consumers.

Some liberty of contract, therefore, in respect to resale prices, seems absolutely essential to any real freedom of competition among manufacturers of trade-marked and branded goods. And so long as such manufacturers in fact compete with each other, and so long as their customers have unrestricted opportunity to pick and choose between rival lines, and to accept or reject the terms upon which they are offered, due regard for the fact that the manufacturers have a real interest in the goods after they have left their hands, and in a very real sense participate in each successive sale down to the ultimate consumer, would seem reasonably to require that they have some degree of right to fix prices in some or all of such sales.